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PAGE 01 STATE 047384

61

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C O N F I D E N T I A L STATE 047384

FOR RALPH BRYANT, HOTEL CRILLON

MEMORANDA FROM YOUR COLLEAGUES FOLLOW: WEDNESDAY, MARCH 14, 1973

ONE - ON CAPITAL CONTROLS

(1) PRINCIPAL US CONTRIBUTION REGARDING CAPITAL FLOWS WOULD BE TO DELAY PHASE OUT OF PRESENT CAPITAL CONTROLS, BY POSTPONING STAGES OF PHASE OUT AND POSSIBLY EXTENDING TERMINATION DATE. RETENTION OF REASONABLY EFFECTIVE US CONTROL PROGRAM WOULD BE TANGIBLE EVIDENCE OF US COOPERATION, WHEREAS ELIMINATION OF CONTROLS MIGHT BE READ AS INDICATING INDIFFERENCE. (2) RELATIVELY SMALL CHANGES IN CONTROLS WOULD BE SIGNIFICANT MAINLY AS SIGNALS OF DIRECTION OF POLICY. MEASURES TO TIGHTEN COULD PROVOKE ANTICIPATORY OUTFLOWS. THUS, RISK OF RAISING IET RATE COULD WELL EXCEED BENEFITS. (IN 1972, TOTAL US OUTFLOWS SUBJECT TO IET WERE A LITTLE LESS THAN THREE- QUARTERS BILLION - PRIMARILY STOCK PURCHASES.) ((3) PROPOSALS TO ENCOURAGE INFLOWS OF SHORT TERM FUNDS INVOLVE WELL KNOWN CONSIDERATIONS. AT PRESENT, US BANKS CAN AGAIN BORROW OVERNIGHT EURODOLLARS AT SMALL COST TO PRESERVE BASES. IF FURTHER EASING IN OVERNIGHT EURO- DOLLAR RATE SHOULD OCCUR THERE MIGHT BE NET INCENTIVE TO BORROW EURODOLLARS RESERVE- FREE.

TWO - ON INTERVENTION

STAFF ASSUMES BASIC THEME IS THAT LARGE SPECULATIVE INFLOWS WOULD
CONFIDENTIAL

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PAGE 02 STATE 047384

BE MET BY CESSATION OF INTERVENTION. IN ABSENCE OF LARGE SPECULATIVE INFLOWS SMOOTHING INTERVENTION MIGHT OCCUR ON RELATIVELY SMALL SCALE, FOR WHICH PRESENT SWAP FACILITIES ADEQUATE. ASSUME THAT US PARTICIPATION WOULD BE FOR PUBLIC PSYCHOLOGICAL VALUE. QUESTIONABLE HOW GREAT THIS VALUE OF SMALL OPERATIONS WOULD BE IF NOT SUPPORTED BY OBJECTIVE DEVELOPMENTS IN BALANCE OF PAYMENTS OVER TIME AS WELL AS BY OTHER ACTIONS DISCUSSED AND REJECTED. ARE SETTLEMENT ARRANGEMENTS VIEWED AS KEY ELEMENT? PUBLIC PSYCHOLOGICAL VALUE PROBABLY LOW.

SMITH ADDS FOLLOWING TO YESTERDAY'S TRUMAN NOTES. QUESTIONS ABOUT SMOOTHING INTERVENTION BY US.

(1) SHOULD WE NOT INTERVENE IN ANY SNAKE CURRENCY MOVING TOO RAPIDLY, WHETHER OR NOT SNAKE MOVING AND WHETHER OR NOT CURRENCY AT LIMIT IN DIRECTION SNAKE MOVING?

(2) WOULD THAT SNAKE COUNTRY ALSO INTERVENE AGAINST DOLLAR?

(3) IF SO, HOW SPLIT INTERVENTION RESPONSIBILITIES? WOULD US BE RESPONSIBLE ONLY FOR NEW YORK MARKET?

THREE - ON SWISS OPTIONS

STAFF VIEW IS THAT MOST LIKELY COURSE THE SWISS WILL FOLLOW IN THE NEAR FUTURE IS TO CONTINUE THE PRESENT UNILATERAL FLOAT. ESTABLISHMENT AND DEFENSE OF A NEW CENTRAL RATE COULD RUN INTO ONE OF TWO DIFFICULTIES, DEPENDING ON WHERE THE RATE WAS SET. SWISS EXPORT INTERESTS ARE COMPLAINING ABOUT THE PRESENT, VERY APPRECIATED RATE OF THE FRANC, AND WHILE IT IS NOT KNOWN HOW MUCH SWISS EXPORTS MIGHT BE DAMAGED BY ANY CONTINUATION OF APPROXIMATELY THE PRESENT EXCHANGE RATE LEVELS THE GOVERNMENT PRESUMABLY WOULD WANT TO AVOID THE RISK OF ANY SEVERE CURRENT ACCOUNT DEFICIT. THE OECD SECRETARIAT HAS PROJECTED APPROXIMATE EQUILIBRIUM IN THE SWISS CURRENT ACCOUNT AT THE PRE- JANUARY 23 EXCHANGE RATES. SETTING A NEW CENTRAL RATE LOWER THAN THE PRESENT FLOATING RATE WOULD RUN THE RISK OF NEW SPECULATIVE INFLOWS, WHICH THE SWISS WISH VERY MUCH TO AVOID. ALTHOUGH BANK CREDIT EXPANSION IS NOW SUBJECT TO CEILINGS, NEW CAPITAL INFLOWS WOULD ADD TO THE MONEY SUPPLY IN THE HANDS OF THE NONBANK PUBLIC AND MAKE IT HARDER TO CONTROL DOMESTIC SPENDING. THE EXTENT OF ANY NEW SPECULATIVE INFLOW MIGHT OF COURSE DEPEND ON HOW THE EC JOINT FLOAT WAS MANAGED.

SWISS HAVE ALREADY CONSIDERED TWO- TIER EXCHANGE MARKET BUT
CONFIDENTIAL

CONFIDENTIAL

PAGE 03 STATE 047384

APPEAR TO HAVE REJECTED IT. RECENT DEVELOPMENTS SHOWING THAT TWO-

TIER SYSTEMS CANNOT PREVENT CAPITAL INFLOWS IN THE FORM OF SHIFTS IN LEADS AND LAGS HAVE PROBABLY FURTHER REDUCED THE CHANCE THAT SWITZERLAND WILL ADOPT SUCH A SYSTEM.

REUTERS REPORTED YESTERDAY THE SWISS NATIONAL BANK AS SAYING SWITZERLAND'S JOINING THE EC JOINT FLOAT IS " OUT OF THE QUESTION." THE EXPERIENCE THUS FAR OF THE " SNAKE" WOULD IN ANY CASE HAVE LED US TO DOUBT ANY SWISS PARTICIPATION IN A JOINT FLOAT.

THE CONTINUATION OF A UNILATERAL FLOAT, WOULD AVOID UNWANTED ADDITIONS TO THE MONEY SUPPLY. AND A DIMINUTION OF SPECULATIVE DEMANDS FOR THE SWISS FRANC WOULD CAUSE THE FRANC TO DEPRECIATE AND THIS WOULD REDUCE THE POSSIBILITY OF DAMAGE TO EXPORT INDUSTRIES. THERE FOLLOWS THE TEXT OF A WIRE JUST RECEIVED BY CHAIRMAN BURNS FROM FINANCE & ECONOMICS MINISTER GISCARD D'ESTAING:

CONTRARY TO INDICATIONS GIVEN IN MY COMMUNICATION OF MARCH 12 THE MEETING OF THE MINISTERS AND CENTRAL BANK GOVERNORS OF THE ENLARGED GROUP- OF- TEN WILL BE HELD FOR REASONS OF CONVENIENCE IN THE PREMISES OF THE OCDE, RUE ANDRE PASCAL IN PARIS AT THE PREVIOUSLY INDICATED HOUR. ROGERS

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